DEC 5

United States General Accounting Office

GAO

Report to the Secretary of Defense

CLASSIFIED

February 1986

COST RECOVERY

Collecting Research and Development Costs on Commercial Military Sales

UNCLASSIFIED ORIGINAL

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GAO

United States
General Accounting Office
Washington, D.C. 20548

National Security and International
Affairs Division
B-214394

February 28, 1986

The Honorable Caspar W. Weinberger
The Secretary of Defense

Dear Mr. Secretary:

We reviewed Department of Defense (DOD) procedures for identifying, monitoring, and collecting nonrecurring research, development, and production costs applicable to commercial sales licensed for export by the Departments of State and Commerce. Nonrecurring costs include such items as special tooling and test equipment, drawings, engineering changes, and product improvements.

Prior internal audits and congressional reports concluded that millions of dollars were lost because effective procedures had not been established. Our review showed that under the present system (1) DOD is not aware of most commercial sales agreements between defense contractors and foreign entities and (2) cannot ensure that recoupments have been collected. Notwithstanding the procedural deficiencies, we found that most of the nonrecurring costs associated with the sales we reviewed were collected by DOD.

In a draft of this report sent to DOD for its comments, we suggested a series of actions to improve the Department's capabilities in this area. Recently, the Department has taken or has proposed taking a number of steps which, although not identical to GAO's recommendations, appear to have the same intent and effect. For the most part, we are satisfied that the Department's approach will address the problems identified in this report, but believe several additional actions would improve the efficiency and effectiveness of DOD's recoupment efforts.

Background

The Arms Export Control Act of 1976 requires a pro rata recovery of dollars spent by the United States for nonrecurring costs associated with the research, development, and production of major defense equipment (MDE) items which are sold under the foreign military sales program to foreign governments or international organizations. Although the act contains no similar requirement to recover a share of these costs on commercial sales by defense contractors or non-MDE, it is DOD policy to do so. In both cases, DOD's objective is to ensure that the purchaser—either government-sponsored or commercial—pays a fair share for the value of DOD's nonrecurring investment costs.

According to DOD directives, any defense item with a government investment of $5 million or more in research, development, test, and evaluation (RDT&E) and production is subject to a nonrecurring cost charge, which is included in the purchase price. Since the U.S. government is not a party to any contractual arrangements for commercial export sales, concerns are that defense contractors may not be collecting and paying the U.S. government a fair share of nonrecurring costs on their commercial sales of defense equipment.

Commercial sales of defense-related articles between U.S. companies and foreign entities or international organizations require U.S. government export licenses. The Department of State issues export licenses for defense items, such as tanks and military aircraft. In addition, many items have both defense and commercial applications. These are termed dual use items, which are licensed for export by the Department of Commerce.

State and Commerce Responsibilities

The Department of State's Office of Munitions Control administers the International Traffic in Arms Regulation, which includes a list of categories of defense articles as designated by the President. An export license must be issued for the sale of items in the categories listed in the regulation. The State Department grants most licenses without consultation with DOD. State refers to DOD for review only those license applications involving special security considerations, sensitive items, or items that are unusual or without precedence. DOD reviews applications to ensure that these exports are in accordance with DOD's policy.

The Department of State approved 28,869 export licenses and manufacturing license/technical assistance agreements received in fiscal year 1983, representing a total of about $10 billion in projected sales. As of September 30, 1985, deliveries made against these approvals amounted to $3.9 billion. The Department approved 33,344 licenses and agreements received during 1984, representing some $12 billion in projected sales. As of September 30, 1985, deliveries against these approvals amounted to about $2.8 billion.

Commerce's Office of Export Administration is responsible for identifying technologies and products that need to be controlled, reviewing and evaluating export license applications, and enforcing export controls.

Under the Export Administration Act, Commerce is authorized to control commercial dual use items. All dual use items requiring U.S. export licenses are included in the Commodity Control List published by Commerce. This list is a composite of items identified unilaterally by the U.S. government and items identified for export control by COCOM for reasons of mutual security. COCOM, or the Coordinating Committee, is an informal organization consisting of the NATO countries (excluding Iceland) plus Japan. This committee controls exports for Communist country destinations.

Most of the commodities on the list are controlled for national security purposes. U.S. exporters refer to the list to find out if commodities they intend to export require licenses. To the maximum extent possible, Commerce unilaterally processes export control applications. DOD is authorized to review and approve those license applications which could affect national security. The vast majority of applications for Commerce export licenses involve low technology products which do not constitute significant military risk. Consequently, DOD reviews relatively few applications except those destined for Communist countries.

Commerce does not maintain records showing the dollar value of export licenses approved or delivered. However, about 116,000 license applications were received, and over 91,000 licenses were approved in calendar year 1984.

DOD's Responsibilities

DOD Directive 2140.2 established the criteria and procedures for the military services, defense agencies, and defense contractors to use when selling products or technology developed with DOD funds to foreign governments, international organizations, foreign commercial firms, or domestic organizations.

The Under Secretary of Defense for Research and Engineering monitors and exercises control over nonrecurring cost recoupments for domestic commercial sales of defense articles and technology. The Assistant Secretary of Defense (Comptroller) provides necessary cost accounting guidance and publishes a list of items or technology for which recoupment charges are applicable. The Director of the Defense Security Assistance Agency (DSAA) is the DOD focal point for reviewing and approving recoupment charges for major defense equipment and for processing recoupment charge waiver requests received from foreign customers.

Recoupment charges are determined by dividing the RDT&E and nonrecurring production cost by the number of units produced and estimated to be produced.

According to the DOD directive, when a U.S. defense contractor negotiates direct sale of a product or technology, the contractor should include in the offer price a nonrecurring recoupment charge. Contractors may request the amount of the charge from the military service responsible for managing the item being exported. The charge for MDE items is developed by the services, approved by DSAA, and published in DSAA's Security Assistance Management Manual. After contractors receive payment they should forward it to the appropriate military service component.

The military services are responsible for identifying and monitoring recoverable costs which should be included in the sales price of commercial exports of defense equipment. The Army depends on receipt of licenses from State and Commerce; the Navy has no formal system for identifying sales; and the Air Force depends on contractors' voluntary compliance.

Results of GAO Review

To determine the adequacy of DOD's procedures in identifying, monitoring, and collecting nonrecurring charges on commercial sales, we reviewed 889 State Department and 52 Commerce export licenses covering fiscal year 1983 shipments. The 889 State licenses were selected using a stratified random sample; the 52 Commerce licenses were judgmentally selected based on high dollar value and likelihood that the item had been developed with DOD research and development funds. We developed two questionnaires—one for industry (app. I) and one for the military service (app. II)—with common questions. In cases where the military service's response disagreed with industry's response, we followed up to resolve the conflicting information.

DOD Was Unaware of Most Commercial Sales

Of the 889 State-issued licenses sampled (out of 12,853 licenses with shipments in fiscal 1983), the military services identified 46 licenses for equipment which carried recoupment charges. Prior to our questionnaire, the military services were not aware of 44 of these State-issued licenses. Applications for only 2 of the licenses had been received by the military service for review.

The military services received none of the 52 Commerce-issued licenses sampled. Most military personnel we spoke to said they had never seen an export license application referred to DOD by Commerce. According to military services, recoupment charges should have applied to 14 of the 52 licenses.

In many instances, the descriptions and nomenclature used on the licenses were not sufficient to determine what precisely was being exported and which service command controlled the item. In about one-third of our sample State licenses, the military services could not identify the appropriate command, or the commands disclaimed responsibility, and in some cases, because of vague or inadequate descriptions, the services had difficulty determining the correct charge. DOD officials informed us that they planned to expand the listing of nonrecurring charges to include commercial nomenclature of derivative items, along with appropriate charges.

Based on our questionnaire experience, we concluded that to review every license would be a very inefficient way to determine recoverable costs of export items—even if State and Commerce sent all the licenses to DOD for review. First, in an overwhelming majority of the cases in our sample, the military services determined that a charge was not applicable. According to the services, about 5 percent of the State licenses in our sample were subject to recoupment charges (46 of 889). A much higher percentage of the Commerce licenses we examined appeared to warrant a charge (14 of 52), but as described on page 4, we purposely biased our sample in that direction.

Our review indicated that reviewing licenses on a selective basis would be the most efficient approach. In our sample cases at State Department, equipment with a shipped value of $1 million or more accounted for 97 percent of the nonrecurring costs which were recovered. On the other hand, licenses with a shipped value of $1 million or more represented about 1 percent of State's issued licenses involving fiscal year 1983 shipments.

Collection Process Needs Improvement

In addition to the 60 State and Commerce licenses identified by the military services as subject to recoupment charges, the contractors identified 5 additional licenses which involved recoverable costs. Shipments had been made under 63 of these 65 licenses. We examined this universe to evaluate collection practices.

Our analysis of the payments relating to the 63 licenses showed that

- the U.S. government was paid most of the money owed in these specific cases;
- the military service records of these payments were incomplete and, in some cases, nonexistent;
- disputes between the services and the contractor over charges were not being resolved expeditiously;
- payments were not made in a timely manner; and
- collection reports were not helpful in monitoring commercial sales payments.

The nonrecurring cost charges for the 63 licenses totalled $7.1 million. (See app. III.) Both the military service and the contractors agreed that about $3.4 million was paid on equipment shipped under 11 licenses.[1]

Contractors told us they had paid an additional $3.4 million on 21 licenses, but the services had no record of the payment. We followed up on these 21 cases, and verified that payments have been made in 8 instances. Subsequently, DOD confirmed that payments had been made in 10 additional cases but had not been recorded.

For the remaining 31 licenses, the contractors and services disagreed over the appropriateness of the charge. The military service identified the total amount due for the 31 licenses as $215,181. In most cases the license applicants either disputed the amount of the charges or said that they had no obligation to pay them.

Disputed Charges

In about half the disputed cases (15 of 31), the contractors maintained there were no obligations for payments because, for example, the item in question had been developed at company expense. In 11 additional cases, the contractors disputed the amount of the charges (the contractors claimed they owed a total of $81,964, while the services said the amount was $126,568). In the remaining cases, we could not determine the specific reasons for nonpayment.

In all disputed cases, the contractors refused to make payment until the dispute was resolved. The largest disputed case involving a State-issued license covered AN/PVS-5 goggles for which $78,340 was owed, according to the military service. The service component had sent a

[1]Includes $71,676 which the contractor paid upon receipt of our questionnaire.

notice to the contractor a year before our study, but the dispute still continued. Meanwhile, the contractor has been making additional sales of these items without paying the DOD component. DSAA has no procedure or requirement to surface and resolve such disputes expeditiously.

Our review of one Commerce-issued license surfaced a major dispute between the contractor and DSAA over the amount of the nonrecurring cost on sales of the CFM 56 engine, a derivative of the F101 engine. If projected sales materialize, $80 million in nonrecurring costs could be involved. A charge of $39,697 for each CFM 56 engine was approved by DSAA in March 1984. However, the contractor claims that (1) a lower charge was negotiated with State in 1973 and (2) the contract between the Air Force and the contractor in 1975 was amended to incorporate a $20,000 charge for each CFM 56 engine. In response to our inquiry, the State Department disavowed knowledge of agreement with the contractor, and pointed out that it did not have the authority to make such an agreement.

DSAA was unaware that the Air Force had concluded a contract that stipulated a lower charge than the one approved by DSAA. As of January 1986, DSAA advised us that the reevaluation of the CFM 56 engine recoupment charge is continuing.

Payments Were Not Timely

DOD Directive 2140.2 does not specify the amount of time a contractor has to make payment to the military services. A DOD Inspector General (IG) report, Financial Reports and Credit Program Division, Defense Security Assistance Agency (No. 84-105, June 28, 1984), stated:

"Collections of revenues due the U.S. government from DOD contractors for the recoupment of nonrecurring costs billed to foreign governments did not comply with good case management practices. DOD had not established standards as to when the contractors should remit the revenues collected from their foreign customers for the recovery of research, development, test and evaluation (RDT&E) costs financed from DOD appropriations."

The IG report showed several instances where contractors submitted payments up to 180 days after delivery of the item. We agree with the IG report conclusion that "Unless nonrecurring costs are collected on a timely basis, the U.S. government will incur unnecessary interest costs." We find merit in the IG's recommendation to change DOD Directive 2140.2 to require payment within 30 days of a sale and subsequently DSAA notified us that an August 1985 revision to DOD Directive 2140.2 requires payment within 30 days.

We also observed several instances where excessive time was required to make payment to the U.S. government. In one instance, a major Army contractor paid recoupment charges on a quarterly basis. Upon examination of the contractor's cash vouchers, we found payment was made almost 150 days after delivery of the items.

For major defense contractors, the military services normally have resident plant representatives to administer government contracts. Their role in the recoupment process has been to receive and forward payments to the military services. U.S. plant representatives were not always timely in forwarding contractors' payments to the appropriate military service. In one case, the military plant representative held the contractor's payment for over 30 days before sending it to the military service. To shorten the processing time, DOD should consider having the defense contractors make payments directly to the military service with a copy of the remittance document provided to the U.S. plant representative.

Collection Report Could Be Improved

DOD's required quarterly report (Form Q1112) shows anticipated and actual collections on direct and foreign military sales and commercial foreign and domestic sales. This report lists the foreign country receiving the equipment and the amount of recoupments due and collected. The report works well for direct government-to-government sales because the recipient government pays the charge to the U.S. government.

The report cannot readily be used to monitor commercial sales because the U.S. defense contractor—not the foreign recipient—makes the payment to the U.S. government. The Q1112 report could be improved for commercial sales monitoring by identifying contractors and the amount of recoupment due and collected on commercial sales.

Based on our evaluation of the Q1112 report, we concluded that listing commercial recoupments by contractors is the most practical way to monitor required payments and collections on commercial sales. The present Q1112 report, which lists recoupments by licenses, is of limited value in monitoring recoupments because contractors frequently make payments without making reference to specific export licenses, and the military services receive few export licenses. Identifying contractors would also provide a means to monitor domestic sales and those other sales that do not require an export license.

We also found that the Army was only reporting collections related to research and development costs and not collections relating to nonrecurring production costs. Both costs should have been reported on Form Q1112 and DOD has recently promulgated instructions to that effect.

New and Improved Procedures Are Needed for Maximum Recovery of Nonrecurring Costs

DOD's efforts to monitor recoupments should begin with identification of those contractors who produce equipment developed with DOD funds. Thus, the monitoring effort should focus on the contractor, rather than on identifying export license applications.

In a draft of this report, we suggested that the government plant representatives—who are located at most of the largest defense plants—could be used as a focal point to provide information to the military service components on contractor sales activity and nonrecurring cost payments. The plant representative could also monitor sales to domestic companies and Canada, which do not require export licenses but are subject to recoupment charges. According to several plant representatives, serving as a focal point for this information would not cause any significant increase in workload.

Subsequent to our review, DOD initiated a proposal to require contractors to notify contracting officers of commercial sales. The proposal was submitted to the Defense Acquisition Council for inclusion in the Federal Acquisition Regulations. DOD reasoned that the responsibility should rest with the contracting officers because they are charged with ensuring compliance with contract terms. As of early January 1986, the Council had not acted on the proposal. Also DOD Directive 2140.2 has recently been revised to require cognizant DOD contract administrative offices to request the Defense Contract Audit Agency to review contractor accounting records to ensure that commercial items were not fully or partly funded by DOD.

Conclusions

At the time of our review DOD did not have a workable system to identify and monitor commercial sales of equipment developed and produced using DOD funds to ensure that appropriate costs are recovered. Essentially the system relied on voluntary payments by contractors. Our sample of licenses indicated that, to a considerable extent, contractors were making the required payments although other problems existed with the process.

DOD needed a system which would meet its management responsibilities, without creating an administrative burden. Key ingredients of the system include presenting available information in a form that can be readily used for these purposes, taking advantage of existing resources to help the services identify sales, selectively targeting export licenses for review, developing procedures to ensure that disputes are surfaced and resolved, and that payments are made timely.

Export license applications could still be used as a management tool to determine whether contractors are reporting all applicable items to the military services—but only on a very selective basis. Rather than attempting to review all licenses, the military services should focus on sales for items having a potential shipped value of $1 million or more. As our review demonstrated, by confining their review to only those sales, the military services could maximize use of review time.

After our field work was completed, DOD initiated several actions to develop a system containing many of the features described above, including (1) proposing a requirement that contractors advise contracting officers of commercial sales, (2) specifying a timeliness standard for payment (30 days), and (3) requiring that nonrecurring production costs be included on the Q1112 report.

The key to DOD's approach is the requirement that contractors notify contracting officers of commercial sales. As of January 1986, this step remains only a proposal and its adoption is critical to the success of DOD's approach.

Several additional actions are needed. First, the usefulness of the Q1112 report would be enhanced if it identified contractors. In that way, the military services would be able to spot delinquent contractors and initiate follow-up action. Secondly, as the services become more efficient in identifying recoupment charges, the need for procedures to surface and resolve disputes will increase. And, lastly, focusing on the sales most likely to yield collections will require cooperation of the Departments of State and Commerce in providing DOD with high value licenses for review.

Recommendations to the Secretary of Defense

We recommend that the Secretary of Defense take action to

- revise the Q1112 report to include contractor identity;
- assure that DSAA and the military departments develop and implement procedures to surface disputes within their respective areas of responsibility; and
- develop procedures, in conjunction with the Secretaries of State and Commerce, requiring that DOD be advised of shipments of more than $1 million.

In the event the proposal before the Defense Acquisition Council is not adopted, we recommend that the Secretary of Defense take steps to ensure that a focal point for monitoring commercial sales—for example the contracting officer or the plant representative—be designated.

Agency Comments

The Departments of Defense and State commented on a draft of this report (see app. IV and V for their detailed responses). The Department of Commerce was asked to comment, but did not respond in time for us to include its comments in this report.

Overall, DOD agreed with the intent of the draft report and concurred fully or partially in most findings and recommendations. DOD pointed out that since our review, DOD had initiated or completed several actions to modify its system for monitoring and collecting nonrecurring costs owed on commercial sales. DOD believes that its actions meet the general objective of our suggested approach and, in any event, should be tried before DOD adopts another change.

For the most part, we agree that the steps taken or proposed should improve DOD's capabilities in this area. DOD's proposal to notify the contracting officer instead of the plant representative of commercial sales is consistent with the intent of the proposal in our draft report, and we have modified our recommendation accordingly.

DOD did not agree with our recommendation to identify contractors on the Q1112 reports. DOD concluded that contractor identity would be an administrative burden and would add little benefit toward monitoring the report. DOD did not explain the basis for its conclusion. We continue to believe that contractor identities would simplify, rather than compound, the collection process. As currently formatted, the Q1112 report was of no use in our effort to follow up on recoupments identified in our sampled cases. It is difficult to identify any significant administrative

burden associated with our proposal, since the information of the Q1112 originates at the contractor. This becomes especially important given DOD's emphasis on contractor compliance with the proposed requirement that contractors advise the contracting officers of commercial sales. An important part of monitoring will be identification on the Q1112 report of those contractors required to report appropriate sales.

Regarding the need for procedures to resolve disputes, DOD concurred on MDE items and stated that the military departments will be advised to notify DSAA of any disputes for MDE items. DOD stated that for non-MDE items, the military departments are responsible for resolving any disputes because they are responsible for establishing the charge. We agree and thus are recommending that the military departments establish procedures for surfacing and resolving conflicts within their area of responsibility.

DOD concurred with our observation that relying on the review of licenses is not a very efficient way to identify recoverable costs. DOD likewise agreed with our recommendation that procedures be developed to ensure that DOD be advised of shipments in excess of $1 million, but the Department stated that it would need State's and Commerce's cooperation to accomplish this.

In its comments, the Department of State agreed to assist DOD in tracing commercial sales by establishing procedures to provide DOD with copies of all high-value export licenses. State also provided updated 1985 statistics, which we have included in the report.

Our review was performed during the period May 1984 to August 1985 in accordance with generally accepted government audit standards.

We are sending copies of this report to appropriate congressional committees; the Secretaries of State and Commerce; the Director, Office of Management and Budget; and other interested parties upon request.

Sincerely yours,

Frank C. Conahan

Frank C. Conahan
Director

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Abbreviations

COCOM	Coordinating Committee
DOD	Department of Defense
DSAA	Defense Security Assistance Agency
GAO	General Accounting Office
IG	Inspector General
MDE	major defense equipment
NATO	North Atlantic Treaty Organization
RDT&E	research, development, test, and evaluation

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Questionnaire Sent to Contractors

U.S. General Accounting Office

SURVEY OF MUNITIONS CONTROL LICENSES

The purpose of this questionnaire is to assess the impact of the Department of Defense's regulation to recoup U.S. government nonrecurring costs associated with the development of defense equipment and technology. You were selected because in 1982 and/or 1983 you were granted an export license(s) for the item in question. This survey is being conducted by the U.S. General Accounting Office, which is responsible for the Congressional oversight of all Federal expenditures and regulatory activities. Specifically we need to track certain licensed items through your accounting controls to see how they are being handled. Also, we need to know what impact, if any, this Defense regulation has had on your competitive position and what parts of this regulation, if any, need to be changed.

Introduction

As you may recall Department of Defense Directive 2140.2 establishes criteria and procedures for use by Department of Defense Components and by United States defense contractors when selling products and technology developed with DOD appropriations/funds to a foreign government, foreign commercial firm, or domestic organization. This applies when the U.S. government invests $5 million or more in research, development, test and evaluation and nonrecurring production to develop technology and related products. The defense contractor must reimburse the U.S. Government for an approved pro-rata charge for the DOD investment costs. Exceptions must have DOD approval. The determination of the $5 million threshold is based upon the end items roll-away, fly-away or sail-way costs. Also, when spare parts packages are sold, recoupments will be made if any component individually meets the $5 million threshold.

We would like to make one thing clear before we continue. This is not an audit of you or your procedures but rather a survey of the population of companies handling licenses. You were selected by chance because you happened to be the licensee for the particular license(s) that was selected at random. Your answers are confidential and will not be used for administrative purposes. Furthermore, the responses will be presented as a collective in summary form, so that no one can tell how you or any other individual company answered. So please give us your most frank and honest answers. We can not make an accurate assessment without your help.

Instructions

The form can be completed in about half an hour if the requested information is readily available. However, in some instances it may take up to a day for decentralized records and retrival systems. Most questions can be answered quickly by checking boxes formatted under license column headings or filling in blanks. However, since the answers will require you to consult your records we suggest that you quickly read the entire form first so that you will have a general idea of what is asked and what types of information you may need from your files.

Please return this completed form in the self-addressed envelope within 10 days after receiving the questionnaire. If you can not meet this time frame or if you have any questions, please call Lou Zanardi or Zachary Jasnoff at (202) 695-1713. They will be standing by to provide assistance. Please help us, we can not assess the impact of this regulation and report your views to the Congress unless we hear from you.

Start card 1 (1) Case no. (2-6)

Column Numbers:	1	2	3	4	5
Lincense Numbers:					
1. The licenses listed in columns 1-5 on the right hand side of the page were selected from the Office of Munition Control records. Check to make sure there are no discrepencies.	(7-12)	(13-18)	(19-24)	(25-30)	(31-36)
1. Country of foreign customers.					
2. Commodity description.	(37-38)	(39-40)	(41-42)	(43-44)	(45-46)
3. Total shipped value in dollars as of February 8, 1984.	(47-49) $	(50-52) $	(53-55) $	(56-58) $	(59-61) $
2. Are there any discrepancies with the information listed above? (Check yes or no for the appropriate column or license number.)	(7-14)	(15-22)	(23-30)	(31-38)	(39-46)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (GO TO 4)	☐	☐	☐	☐	☐
3. No basis to judge (GO TO 4)	☐	☐	☐	☐	☐
3. If yes, please make the corrections in the space provided below.	(47)	(48)	(49)	(50)	(51)
1. Country of foreign customers.	(7-8)	(9-10)	(11-12)	(13-14)	(15-16)
2. Commodity description.	(17-19)	(20-21)	(22-25)	(26-28)	(29-31)
3. Shipped value in dollars.	$	$	$	$	$
4. Is a recoupment charge for R&D and nonrecurring production costs applicable to this license?	(32-39)	(40-47)	(48-55)	(56-63)	(64-71)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (GO TO 10)	☐	☐	☐	☐	☐
	(72)	(73)	(74)	(75)	(76)

Start card 4 (1) Case no. (2-6)

Column Numbers:	1	2	3	4	5
License Numbers:					
5. If yes for any of the licenses listed in columns 1-5, what is the amount of the recoupment charge? (Write the total amount of the charge in dollars under the appropriate column)	$	$	$	$	$
6. Has your company included the nonrecurring recoupment charge in the offering price?	(7-13)	(14-20)	(21-27)	(28-34)	(38-41)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (GO TO 8)	☐	☐	☐	☐	☐
7. Again if yes to any licenses in question 4, did you directly notify the appropriate Department of Defense component of the sale and the recoupment charge to be collected.	(42)	(43)	(44)	(45)	(46)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (CONTINUE)	☐	☐	☐	☐	☐
8. If the nonrecoupment charge was applicable, was it collected from the customer?	(47)	(48)	(49)	(50)	(51)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (CONTINUE)	☐	☐	☐	☐	☐
9. Regardless of whether you collected the charges, was payment made to the appropriate DOD component?	(52)	(53)	(54)	(55)	(56)
1. Yes (CONTINUE)	☐	☐	☐	☐	☐
2. No (CONTINUE)	☐	☐	☐	☐	☐
	(57)	(58)	(59)	(60)	(61)

Start card 9 (1) Case no. (2-6)

Column Numbers:	1	2	3	4	5
License Numbers:					
10. If you answered no to any license in question 4, indicating that the recoupment charge was not applicable, why no? (Check the appropriate column(s) for the rows that best explain your reasons.) (SKIP TO 11 for those columns to which you answered yes in question 4.					
1-None of the items offered met the $5 million threshold requirement.	☐ (7)	☐ (8)	☐ (9)	☐ (10)	☐ (11)
2-Did not have a way to determine if $5 million or more of R & D and nonrecurring production cost was invested in the item.	☐ (12)	☐ (13)	☐ (14)	☐ (15)	☐ (16)
3-Company did not develop or produce items exported.	☐ (17)	☐ (18)	☐ (19)	☐ (20)	☐ (21)
4-Company does not believe it has a contractual obligation to pay the recoupment charges.	☐ (22)	☐ (23)	☐ (24)	☐ (25)	☐ (26)
5-Item offered probably met the $5 million threshold, but DOD has not developed the pro rata charge associated with the item.	☐ (27)	☐ (28)	☐ (29)	☐ (30)	☐ (31)
6-Item was purchased from another company which included the recoupment charge. (If checked, specify the company and the amount of the charge in dollars.)	☐ (32)	☐ (33)	☐ (34)	☐ (35)	☐ (36)
1. Company					
2. Amount of charge in dollars.	(37-39) $	(40-42) $	(43-45) $	(46-48) $	(49-51) $
7-Item was purchased from another company and we could not determine if a recoupment charge was added.	(52-55) ☐ (57)	(56-59) ☐ (58)	(60-63) ☐ (59)	(64-67) ☐ (60)	(68-71) ☐ (61)
8-Payment waived by DOD.	☐ (62)	☐ (63)	☐ (64)	☐ (65)	☐ (66)
9-Other (Specify)	(67)	(68)	(69)	(70)	(71)

Start card 7 (1) Case no. (2-6)

Column Numbers:	1	2	3	4	5
Licenses Numbers:					
11. What was your role in developing, manufacturing and selling the item or related units? (Check the appropriate row in column of the license you are answering for.)					
1. Involved in developing, manufacturing and selling.	☐ (7)	☐ (8)	☐ (9)	☐ (10)	☐ (11)
2. Involved in manufacturing and selling but not developing.	☐ (12)	☐ (13)	☐ (14)	☐ (15)	☐ (16)
3. Involved in developing and selling but not manufacturing.	☐ (17)	☐ (18)	☐ (19)	☐ (20)	☐ (21)
4. Just the seller.	☐ (22)	☐ (23)	☐ (24)	☐ (25)	☐ (26)
5. Export agent for a purchasing country.	☐ (27)	☐ (28)	☐ (29)	☐ (30)	☐ (31)

GENERAL INFORMATION

12. Has your company paid a recoupment charge to the U.S. government in the last five years?

1. [__] Yes (32)
2. [__] No
3. [__] No basis to judge

13. To what extent, if at all, did the requirement to recoup nonrecurring costs impact on your business? Answer for each of the following types of impact. (Check one column for each row.)

	1. To little or no extent	2. To some extent	3. To a moderate extent	4 To a great extent	5. To a very great extent	
1. Decrease business						(33)
2. Decrease profit margin						(34)
3. Increase overhead burden						(35)
4. Decrease competitive position						(36)
5. Increase marketing burden						(37)
6. Other (Specify) _____ _____						(38)

14. Were you aware that under certain circumstances waivers from collecting nonrecurring costs can be granted for sales to NATO countries, Australia, New Zealand and Japan?

1. [__] Yes (39)
2. [__] No

15. Do you think the U.S. government is more or less likely to grant waivers to a foreign buyer when the U.S. government makes a foreign military sale, than it is to grant a waiver when a U.S. firm makes a direct commercial sale? (Check one) (40)

1. [__] Much less likely to grant waivers when the government makes a sale instead of a U.S. firm making a direct commercial sale.
2. [__] Less likely to great waivers when the government makes a sale instead of a U.S. firm making a direct commercial sale.
3. [__] Just as likely to grant waivers when the government makes a sale instead of a U.S. firm making a direct commercial sale.
4. [__] More likely to grant waivers when the government makes a sale instead of a U.S. firm making a direct commercial sale.
5. [__] Much more likely to grant waivers when the government makes a sale instead of a U.S. firm making a direct commercial sale.
6. [__] No basis to judge.

16. What threshold, if any, should be applied to R and D and nonrecurring production costs? (Check one.) (41)

1. [__] 0, or no threshold, all nonrecurring costs should be recouped no matter how great or small.

2. [__] Threshold should be lowered to $2 million.

3. [__] Threshold should remain at $5 million.

4. [__] Threshold should be raised to $10 million.

5. [__] Threshold should be raised to $20 million.

6. [__] Threshold should be raised to $30 million.

7. [__] Threshold should be raised to $40 million.

8. [__] Threshold should be r 4 to $50 million.

9. [__] Threshold should be raised to over $50 million.

10. [__] No nonrecurring costs should be recouped.

17. Some people believe that the current methods used to recoup investment costs have significantly increased the sales price beyond the reasonable market price. They believe that DOD should have the flexibility to cap recoupment charges when current methods impede the sale. In these instances, the capping price would be based on a percent of the sale. Others disagree on the bases that this would be unfair to other U.S. companies and/or create loopholes. The question is do you agree or disagree with the proposal to give the government the flexibility to cap the recoupment charges. (42)

1. [__] Strongly agree

2. [__] Generally agree

3. [__] Agree as much as disagree

4. [__] Generally disagree

5. [__] Strongly disagree

18. Some companies believe that the U.S. government should exercise flexibility and grant waivers when a sale may be lost because of a large recoupment charge. Again others disagree arguing that waivers should be granted only when it is in the U.S. national interests (e.g., standardization of equipment among allies, etc.) They claim waivers should not be granted in most cases because competition is likely to come from U.S. companies which have used their own resources to develop competing equipment. The question is do you agree or disagree with the proposal to give government more flexibility to grant waivers including waivers for cases where a sale may be lost because of a large recoupment charge?

(43)

1. [__] Strongly agree

2. [__] Agree

3. [__] Agree as much as disagree

4. [__] Disagree

5. [__] Strongly disagree

19. If you have any thoughts or additional information about any of the issues covered by this questionnaire please feel free to comment. Also if you have any comments about questions that you feel we should have asked but did not, we would like to know.

(44)

Questionnaire Sent to the Military Services

U.S. General Accounting Office

SURVEY OF MUNITIONS CONTROL LICENSES

Introduction

The purpose of this questionnaire is to assess the impact of the Department of Defense (DOD) effort to recoup U.S. government nonrecurring costs associated with the development of defense equipment and technology. You were selected because in 1982 and/or 1983 you may have reviewed an export license application for the item in question. This survey is being conducted by the U.S. General Accounting Office, which is responsible for the congressional oversight of all federal expenditures and regulatory activities.

The questionnaire is administrated in three parts. In part I, we want to determine if the appropriate DOD component is aware of the license and whether the license has been tracked through your accounting records. In part II, we want to know if a pro rata charge is applicable to the license and if it has been collected. In Part III, we ask general questions to assess possible staffing requirements needed to increase DOD efforts to recoup nonrecurring investment costs. Part III will be completed by the commanding officer of the DOD component receiving the questionnaires.

As you may recall, DOD Directive 2140.2 establishes criteria and procedures for use by DOD components and by U.S. defense contractors when selling products and technology developed with DOD appropriations/funds to a foreign government, foreign commercial firm, or domestic organization. This applies when the U.S. government invests $7 million or more in research, development, test and evaluation, and nonrecurring production to develop technology and related products. The defense contractor must reimburse the U.S. government an approved pro rata charge for the DOD investment costs. Exceptions must have DOD approval. The determination of the $5 million threshold is based upon the end items roll-away, fly-away, or sail-away costs. Also, when spare parts packages are sold, recoupments will be made if any component individually meets the $5 million threshold.

We would like to make one thing clear before we continue. This is not an audit of you or your procedures but rather a survey of the population of licenses. You were selected by chance because you happened to be responsible for reviewing the particular license(s) that was selected at random. The sample universe consists of licenses for which shipment has been made. Your answers are confidential and will not be used for administrative purposes. Furthermore, the responses will be presented in summary form so that no one can tell how you or any other individual DOD component answered. So please give us your most frank and honest answers. We cannot make an accurate assessment without your help.

Instructions

The form can be completed in about half an hour if the requested information is readily available. However, in some instances it may take up to a day for decentralized records and retrieval systems. Most questions can be answered quickly by checking boxes formatted under license column headings or filling in blanks. However, since the answers will require you to consult your records, we suggest that you quickly read the entire form first so that you will have a general idea of what is asked and what types of information you may need from your files.

Please disregard the small numbers in parentheses under the columns and in the right margins. They are for data processing purposes.

NAVY: If the necessary information to answer any question is not in your office, we would like you obtain it from the appropriate office. Therefore, we request that certain questions be coordinated with and answered by the appropriate Plant Representative Office.

Please return this completed form in the self-addressed envelope within 10 days after receiving the questionnaire. If you cannot meet this timeframe or if you have any questions, please call Lou Zanardi or Ed Kennedy at (202) 695-1713. They will be standing by to provide assistance. Please help us, as we cannot assess the impact of this regulation and report your views to the Congress unless we hear from you.

Part I: Verifying License Data

ocart card 1 (1)
case no. (2-6)

Column Numbers:	1	2	3	4	5
License Numbers:					
1. The licenses listed in columns 1-5 on the right-hand side of the page were selected from the Office of Munition Control records. The license information in rows 1, 2, & 3 describes the areas covered by the license. 1. Country of foreign customers. 2. Commodity description. 3. Shipped value.	(7-12)	(13-18)	(19-24)	(25-30)	(31-36)
	SEE ATTACHED LICENSE(S)				
2. Does this license contain articles and/or services controlled by your organization? (Check yes or no for the appropriate column or license number.)					
1. Yes (Continue for this license.)	☐	☐	☐	☐	☐
2. No (Stop for this license.)	☐	☐	☐	☐	☐
3. Does your organization have a record of the license application on file? (Check yes or no for each column or license.)	(37)	(38)	(39)	(40)	(41)
1. Yes (If yes, continue for this license.)	☐	☐	☐	☐	☐
2. No (If no, go to 7 for this license.)	☐	☐	☐	☐	☐
4. Does the record indicate that the license has been approved by the Office of Munitions Control?	(42)	(43)	(44)	(45)	(46)
1. Yes	☐	☐	☐	☐	☐
2. No	☐	☐	☐	☐	☐
	(47)	(48)	(49)	(50)	(51)

Column Numbers:	1	2	3	4	5
License Numbers:					
5. Does the record indicate that the article or services have been exported? 1. Yes 2. No	☐ ☐	☐ ☐	☐ ☐	☐ ☐	☐ ☐
6. Which of the following information sources provided the bases for establishing a record for this article or service(s)? (Check all that apply.)	(52)	(53)	(54)	(55)	(56)
1. Services review was required during coordinations with Department of State and/or during other DOD component approval process.	☐ (57)	☐ (58)	☐ (59)	☐ (60)	☐ (61)
2. Contractor notified your organization items to be exported through payment.	☐	☐	☐	☐	☐
3. License previously selected through an internal audit and its review.	(62) ☐	(63) ☐	(64) ☐	(65) ☐	(66) ☐
4. Other (Specify in column space) 1. _____ 2. _____ 3. _____ 4. _____ 5. _____	(67) ☐	(68) ☐	(69) ☐	(70) ☐	(71) ☐
	(72)	(73)	(74)	(75)	(76)

Part: II Collecting Nonrecurring Cost (NRC) recoupment charges

7. Are NRC recoupment charges applicable to the licensed item identified in the above column?				start card 2 (1) case number (2-6)	
1. Yes (If yes, go to 9 for this license.)	☐	☐	☐	☐	☐
2. No (If no or undecided, continue to 8, then stop for this license.)	☐	☐	☐	☐	☐
3. Undecided.	☐	☐	☐	☐	☐
	(17)	(18)	(19)	(20)	(21)

Column Numbers:	1	2	3	4	5
License Numbers:					
8. If no, why are NRC recoupment charges not applicable? (Check all that apply, then stop for this license.)					
1. Item was developed without government funding.	☐ (22)	☐ (23)	☐ (24)	☐ (25)	☐ (26)
2. Item was developed with U.S. funds but did not meet $5 million R&D threshold.	☐ (27)	☐ (28)	☐ (29)	☐ (30)	☐ (31)
3. License involves only spare parts or components which do not qualify separately as items meeting $5 million threshold.	☐ (32)	☐ (33)	☐ (34)	☐ (35)	☐ (36)
4. A legal basis for collection may not exist because basic clause from DAR 7-104.64 on recovery of nonrecurring costs was not included in contract.	☐ (37)	☐ (38)	☐ (39)	☐ (40)	☐ (41)
5. Other (specify in column space) 1. _____ 2. _____ 3. _____ 4. _____ 5. _____	☐ (42)	☐ (43)	☐ (44)	☐ (45)	☐ (46)
6. No basis to judge. Remember stop for this license if you answered 8.	☐ (47)	☐ (48)	☐ (49)	☐ (50)	☐ (51)
9. If an NRC recoupment charge is applicable, please list the charge per unit and the total charge for the sale.				start card 3 (1) case no. (2-6)	
1. Charge/unit.	$ (7-13)	$ (14-20)	$ (21-27)	$ (28-34)	$ (35-41)
2. Total charge due on license.	$ ____	$ ____	$ ____	$ ____	$ ____
10. Has the amount of the NRC recoupment charge been approved, or is it pending?	(42-48)	(49-55)	(56-62)	(63-69) start card 4 (1) case no. (2-6)	(70-76)
1. Approved (If approved, go to 12 for this license.)	☐ (7)	☐ (8)	☐ (9)	☐ (10)	☐ (11)
2. Pending (If pending, continue for this license.)	☐ (12)	☐ (13)	☐ (14)	☐ (15)	☐ (16)

Column Numbers:	1	2	3	4	5
License Numbers:					
11. If the amount of the NRC charge is pending, what are the reasons? (Check one or more.)					
1. Command has submitted the pro rata NRC recoupment charge, but DSAA has not approved it.	☐ (17)	☐ (18)	☐ (19)	☐ (20)	☐ (21)
2. The recoupment cost data is not available.	☐ (22)	☐ (23)	☐ (24)	☐ (25)	☐ (26)
3. The recoupment cost data is available but pro rata charge not developed.	☐ (27)	☐ (28)	☐ (29)	☐ (30)	☐ (31)
4. Determination is complicated and requires several months of work.	☐ (32)	☐ (33)	☐ (34)	☐ (35)	☐ (36)
5. Have been working on the determination a short time (3 months or less).	☐ (37)	☐ (38)	☐ (39)	☐ (40)	☐ (41)
6. Other (specify in column space) 1. _____ 2. _____ 3. _____ 4. _____ 5. _____	☐ (42)	☐ (43)	☐ (44)	☐ (45)	☐ (46)
7. No basis to judge.	☐ (47)	☐ (48)	☐ (49)	☐ (50)	☐ (51)
12. Has your organization advised the vendor of the recoupment charges?					
1. Yes (If yes, go to 14 for this license.)	☐	☐	☐	☐	☐
2. No (If no, continue for this license.)	☐	☐	☐	☐	☐
	(57)	(58)	(59)	(60)	(61)

start card 5 (1)
case no. (2-6)

Column Numbers:	1	2	3	4	5
License Numbers:					
13. If no, indicate the reasons for not advising the vendor and skip to 19.					
1- Recipient has a waiver for the charges.	☐ (7)	☐ (8)	☐ (9)	☐ (10)	☐ (11)
2- Your organization was not aware that the license had been approved.	☐ (12)	☐ (13)	☐ (14)	☐ (15)	☐ (16)
3- Heavy work load has made it difficult to advise vendor in a timely fashion.	☐ (17)	☐ (18)	☐ (19)	☐ (20)	☐ (21)
4- Other (specify in column space.)	☐ (22)	☐ (23)	☐ (24)	☐ (25)	☐ (26)
1. _____ 2. _____ 3. _____ 4. _____ 5. _____					
NOTE: Remember if you answered 13, skip to 19.					
14. Has the vendor agreed, disagreed, or not commented on the charges?	☐	☐	☐	☐	☐
1. Agreed.	☐	☐	☐	☐	☐
2. Disagreed.	☐	☐	☐	☐	☐
3. Not commented.	☐ (37)	☐ (38)	☐ (39)	☐ (40)	☐ (41)
15. What amount if any of the NRC recoupment charge has been paid?				start card 6 (1) case no. (2-6)	
1. Full amount (CONTINUE).	☐ (7)	☐ (8)	☐ (9)	☐ (10)	☐ (11)
2. Partial amount (write the $ amount in column space and continue for this license.) (CONTINUE)	$ (12-18)	$ (19-25)	$ (26-32)	$ (33-39)	$ (40-46)
3. None (Go to 17 for this license.)	☐	☐	☐	☐	☐
	(47)	(48)	(49)	(50)	(51)

Column Numbers:	1	2	3	4	5
License Numbers:					
16. Approximately how many weeks did it take to collect at least some of the NRC recoupment charges?	(weeks) (52-53)	(weeks) (54-55)	(weeks) (56-57)	(weeks) (58-59)	(weeks) (60-61)
17. How many inquiries, follow-ups, or attempts, if any, were made to collect the NRC recoupment charge? (Number of inquiries or follow-ups.)	No.___ (62)	No.___ (63)	No.___ (64)	No.___ (65)	No.___ (66)
18. Approximately how many weeks has it been since the vendor was advised of the NRC recoupment charge for this license?	(weeks) (67-68)	(weeks) (69-70)	(weeks) (71-72)	(weeks) (73-74)	(weeks) (75-76)

19. If you have any thoughts or additional information about any of the issues covered in this questionnaire, please feel free to comment. Also, if you have any comments about questions that you feel we should have asked but did not, we would like to know them. (WRITE YOUR ANSWERS IN THE SPACE BELOW OR ON THE BACK OF THIS PAGE.)

(77-78)

Thank you for completing Parts I and II of this questionnaire for the licences listed.

Payments Status for Sample Cases With Identified Recoupment Charge

Status	Cases	Amount
DOD and contractor agree payment made	11	$3,444,483
Contractor claims payment[a] but DOD initially unable to confirm	21	3,453,203
Disputed charges	31	215,181
Total	**63**	**$7,112,867**

[a]We followed up on 8 of the 21 cases in this category and verified that payments were made. Subsequently, DOD confirmed in another 10 cases that payments were made. The remaining cases involved 3 cases where the services' component indicated that a charge was not owed.

Advance Comments From the Department of Defense

DEFENSE SECURITY ASSISTANCE AGENCY

WASHINGTON D.C. 20301-2800

5 DEC 1985

In reply refer to:
I-16034/85

Mr. Frank C. Conahan
Director
National Security and International Affairs Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Conahan:

This letter provides the Department of Defense (DoD) response to draft GAO report, "Problems in Identifying, Monitoring, and Collecting Nonrecurring Charges Owed to the U.S. Government", dated September 27, 1985, GAO code number 463718, OSD case number 6546.

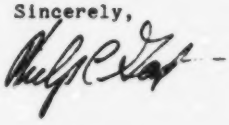
The DoD position on each Finding and Recommendation in the report is enclosed.

The DoD generally agrees with the intent of the Findings and Recommendations in the draft report. However, numerous actions are underway or have been completed which modify the DoD system for the identification, reporting, and collection of charges due the DoD from the direct commercial sale of defense items. While the actions do not precisely follow the GAO recommendations, they will improve the monitoring and collection of non-recurring recoupment costs owed the U.S., which should meet the GAO stated objectives. Expanded guidance and procedures were included in the revision to DoD Directive 2140.2, which was published on 5 August 1985. Further, in late 1984, the Defense Security Assistance Agency (DSAA) initiated action with the Office of the Under Secretary of Defense for Research and Engineering (OUSDR&E), the Office of the Assistant Secretary of Defense (Acquisition and Logistics) (OASD A&L)) and the Defense Acquisition Regulatory (DAR) Council to publish necessary provisions in the DoD Federal Acquisition Regulation (FAR) Supplement. These provisions will require reporting of commercial sales to the DoD contracting officer. This action is currently in progress.

The DoD does not agree with GAO's recommendation to include contractor names in the Q1112 Report. To do so would involve an administrative burden, and would not result in any substantive identifiable benefit.

The DoD actions have been responsive to the GAO intent. Most of the GAO concerns in fact, have been resolved. It should be noted, however, that in certain areas DoD's ability to completely implement the necessary system changes is contingent on the continued support from the Departments of State and Commerce in providing information on approved export licenses.

Sincerely,



Attachments
as stated

PHILIP C. GAST
LIEUTENANT GENERAL, USAF
DIRECTOR

FINDINGS

FINDING A: The Department of Defense (DoD) Does not Have a Workable System To Ensure Appropriate Non Recurring Costs Are Recovered From Sales to Foreign Customers. The GAO found that it is DoD policy to recover a pro rata share of its nonrecurring costs (associated with research and development, and production) from commercial sales of weapon systems, where such nonrecurring costs exceed $5 million per system (and where no waiver is applicable). However, the GAO found that, for collecting such charges in sales to foreign customers, current procedures rely upon review of export licenses and upon voluntary compliance by contractors. Based upon its analyses of the results of questionnaires submitted to the Services and to industry, the GAO concluded that DoD does not have a workable system to identify and monitor commercial sales of equipment developed and produced using DoD funds to ensure that appropriate costs are recovered. (pp. 1, 2, 5, 6 and 14, GAO Draft Report).

Now on pp. 1-5 and 8-9

DoD Position: Partially concur. This was partially true at the time the GAO conducted the review; however, since then a number of specific actions not mentioned in the report have been accomplished. First, action was initiated by DSAA with OUSDR&E/ASD(A&L) and the DAR Council to publish guidance in the DoD FAR Supplement for contracting officers, and also to require industry to advise the contracting officer of all commercial sales of U.S. Government developed defense items and applicable derivative items. Second, on August 5,1985, DoD published a complete revision of DODD 2140.2, Recoupment of NRC on Sales of U.S. Products and Technology. The revised Directive establishes a new system and revised guidance in this area. It should also be noted that DoD must rely on other U.S. Government Agencies for copies of license approvals. The cooperation of both the Departments of State and Commerce is essential in this effort.

FINDING B: Reliance Upon DoD Review of Export Licenses Inefficient Way to Determine Recoverable Costs. The GAO found that the Office of Munitions Control of the Department of State (State) issues export licenses for defense articles and services designated in the International Traffic in Arms Regulations. On the other hand, the Office of Export Administration of the Department of Commerce (Commerce) issues export licenses for dual use items (that have both defense and commercial application) listed in the Commodity Control List. The GAO found that State consults DoD on only those license applications involving special security considerations, sen-

sitive items, or items that are unusual or without precedent, and that DoD reviews very few Commerce license applications except those destined for communist countries. The GAO included, in its questionnaire to the Services, samples of licenses issued by State and Commerce covering 1983 shipments. Of some 46 State licenses which the Services identified as carrying recoupment charges, only 2 had been previously sent to the Services for review, and none of the 52 Commerce license in the GAO sample had been seen. The GAO also found that in an overwhelming majority of cases in its sample (843 of 889 State licenses--selected as a stratified random sample--and 38 of 52 Commerce licenses--selected for high dollar value and likelihood of DoD nonrecurring costs) the Services determined that a charge was not applicable. In addition, the GAO found that the descriptions and nomenclature used on the licenses were not sufficient to determine what precisely was being exported and which Service command controlled the item. For instance, on about one third of the GAO sample of State licenses, the Services could not ascertain which command was responsible. Furthermore, in some cases, because of vague or inadequate descriptions, the Services had difficulty determining the correct charges. The GAO concluded that the same problems would occur--only on a vastly increased scale--if DoD attempted to track recoupment charge payments based on review of all licenses (estimated to be about 180,000 per year for State and Commerce combined.) The GAO concluded, further, that relying on DoD's review of licenses is a very inefficient way to determine recoverable costs of export items. (pp. 2-4, 6 and 7, GAO Draft Report).

Now on pp 2-5

DoD Position: Concur. The DoD agrees with GAO's conclusion that relying on the review of licenses is a very inefficient way to determine recoverable costs. The alternatives being reviewed will result in further system improvements. (See, also, DoD response to Findings A, D and E.)

FINDING C: Collection Process and Collection Report Need Improvement. The GAO evaluated collection practices for the 63 licenses in its sample that were subject to collection of nonrecurring costs (60 identified by the Services and 5 more identified by contractors--of which 63 involved shipments). The GAO found, among other things, that for these cases the U.S. Government was paid most of the money owed but that the Service' records of payment were incomplete. The GAO found that the applicable nonrecurring cost charges for the 63 licenses totalled $7.1 million; that both the Services and the contractors agreed that about $3.4 million was paid on equipment shipped under 11 licenses; but that contractors identified an additional $3.4 million they had paid on 21 licenses, of which the Services had no record, or which GAO could not verify from

the Services' records. Only on follow-up was the GAO eventually able to verify receipt by the Services. (In addition $.2 million was in dispute). The GAO also looked at the DoD quarterly report (Form Q 1112), which shows anticipated and actual collections. This report lists the foreign country receiving the equipments and the recoupments due and collected. However, the GAO found that the report cannot readily be used to monitor commercial sales because the U.S. defense contractor--not the foreign recipient--makes payments to the U.S. Government. In addition, the GAO found that the Army is only reporting collections related to RDT&E, and not to production. The GAO concluded that the Q 1112 report could be improved for commercial sales monitoring by identifying therein contractors and the amount of recoupment due and collected on commercial sales. (pp. 7, 8, and 11, GAO Draft Report).

Now on pp. 5-6 and 8-9

DoD Position: Partially Concur. Nonconcur with the expansion of the report to include identification of the contractors. This would be an administrative burden with little or no benefit towards monitoring the report. Concur in adding the nonrecurring production costs. This change has been promulgated in DOD Directive 2140.2.

FINDING D: Government Plant Representative--Use As Focal Point For Monitoring. The GAO found that DoD's efforts to monitor recoupments should begin with identification of those contractors who produce equipment, and thus, that the focus for the DoD monitoring effort for recovery of nonrecurring costs should be directed at the plant facilities manufacturing applicable equipment, rather than at identifying export license applications. The GAO concluded that the Government plant representatives easily could be used to provide information to the Service components on contractor sales activity and on nonrecurring cost payments, after noting that several plant representatives indicated this would not cause any significant increase in workload. (The GAO also noted that, as an added benefit, these plant representatives could monitor sales to domestic companies and to Canada.) (pp. 13 and 14, GAO Draft Report).

Now on p. 9

DoD Position: Partially Concur. After the GAO completed its review, the DoD took action through OUSDR&E, ASD(A&L) and the DAR Council to provide for DoD FAR Supplement coverage for notification of commercial sales to the contracting officers, rather than plant representatives as suggested by the GAO. The contracting officers have overall responsibility for ensuring compliance with contract terms. This action meets the general objective of this Finding and, in any event, should have an opportunity to succeed before the DoD adopts a further change.

FINDING E: Selective Review of License Applications. The GAO found that export license application could be used as a management tool to determine whether contractors are reporting all applicable items to the Services--but only on a very selective basis. The GAO, in its sample of State cases, found that equipment with a shipped value of $1 million or more accounted for 97

Now on pp. 5 and 10.

percent of the value of nonrecurring costs, but only about 1 percent of the number of licenses involving fiscal year 1983 shipments. The GAO concluded that by selectively targeting licenses having a potential shipped value of $1 million or more, rather than attempting to review all licenses, the Services could make maximum use of review time. (pp. 13 and 14, GAO Draft Report).

DoD Position: Concur. It must be recognized that DoD needs the cooperation of the Departments of State and Commerce to provide these licenses for review. This cannot be unilaterally accomplished within DoD.

FINDING F: Disputed Charges And Dispute Procedures. In its sample of export licenses the GAO found 31, amounting to $215,181 in potential recoupments, wherein the contractor and the Service disagreed over the charge. In 15 of 31 cases the contractor maintained there was no obligation because, for example, the item had been developed at company expense. In 11 additional cases the amounts (contractor $81, 964--Services $126,568) were in dispute. (The GAO could not determine the cause of nonpayment in the remaining 5 cases.) The largest State licensed item which GAO found to be under dispute involved AN/PVS-5 goggles, for which the Service component had sent a notice, a year earlier, to the contractor claiming $78,340, which had not been paid. The GAO found that the contractor, meanwhile, had been making additional sales of these goggles, again without paying. The GAO found that DSAA had no procedure or requirement to surface and resolve such disputes expeditiously. In addition, the GAO review of a Commerce license for CRM66 engines surfaced a major dispute. If projected sales of this F101 engine derivative materialize, the GAO found that $80 million in nonrecurring costs could be involved. The GAO also found that a charge of $39,697 per engine was approved by DSAA in March 1984. However, the contractor claims that a lower charge was negotiated with State in 1973, and the Air Force contract was amended in 1975 to include a charge of $20,000 for each engine. The GAO reported that State disavowed knowledge of an agreement with the contractor, and pointed out that it did not have authority to make such an agreement. The GAO found the DSAA was unaware that the Air Force had stipulated the lower charge and DSAA advised, in June 1985, that it was reevaluating the CRM engine recoupment charge. The GAO concluded that procedures should be developed to ensure that disputes are surfaced to DSAA and resolved. (pp. 8-10, and 14, GAO Draft Report).

Now on pp. 6-7 and 10.

DoD Position: Partially concur. To the extent that there is a dispute on the amount of a charge for a Major Defense Equipment (MDE) item, such disputes will be surfaced to DSAA. DSAA will advise the Military Departments to do this. DoD Directive 2140.2 provides for the Military Department to establish charges for non-MDE items. Any dispute on the amount of a charge for a non-MDE item, therefore, must be resolved by the Military Department that determined the charge.

Now on pp. 7-8 and 10

FINDING G: Payments Are Not Timely. The GAO found that DoD Directive 2140.2 does not specify the timing of contractor payments to the Services. (This was noted in DoD Inspector General (IG) Report No. 84-105, June 28, 1984, which found that revenue collection was not managed properly, as DoD had not established standards for when contractors should pay.) The GAO agreed with the conclusion of the IG report that, "Unless nonrecurring costs are collected on a timely basis, the U.S. Government will incur unnecessary interest costs." The GAO also observed several instances where payments were too slow, or in which U.S. plant representatives forwarded payments too slowly. The GAO concluded that the DoD IG recommendation to change DoD Directive 2140.2 to require payment within 30 days or a sale had merit. The GAO also concluded that DoD should consider having defense contractors make payments directly to the Services with a copy to the U.S. plant representative. (pp. 8, 10, 11, and 14, GAO Draft Report).

DoD Position: Partially Concur. At the time of the GAO audit, guidance did not specify timing of contractor payments. However, since the GAO audit, revised guidance has been disseminated in revised DOD Directive 2140.2, dated 5 August 1985. The revised Directive requires payment within 30 days.

RECOMMENDATIONS

RECOMMENDATION 1: The GAO recommended that the Secretary of Defense implement revision of Form Q1112 to include contractor identity and nonrecurring production costs on commercial sales. (p. 15, GAO Draft Report).

Now on p. 11.

DoD Position: Partially Concur. Nonconcur with the expansion of this report which would be an administrative burden of little or no benefit. Concur in adding non-recurring production costs, and in fact have already done so.

RECOMMENDATION 2: The GAO recommended that the Secretary of Defense require U.S. Government plant representatives to obtain from the contractor completed sales cases and forward this information to the appropriate Services. (p. 15, GAO Draft Report).

Deleted, see pp. 9 and 11.

DoD Position: Partially concur. Action has already been initiated through OUSDR&E, ASD(A&L) and the DAR Council to provide for DoD FAR Supplement coverage for notification of commercial sales to the contracting officer. This action should meet the intent of the GAO recommendation. (See, also, the DOD response to Finding D.)

Recommendation 3: The GAO recommended that the Secretary of Defense, in cooperation with the Secretaries of State and Commerce, develop procedures requiring that copies of all licenses that involve shipments of more than $1 million be forwarded to the appropriate Service. (p. 15, GAO Draft Report).

Now on p. 11.

DoD Position: Concur. It must be recognized that DoD needs the cooperation of the Department of State and Commerce to accomplish this recommendation. This cannot be unilaterally accomplished within DoD.

Recommendation 4: The GAO recommended that the Secretary of Defense develop and implement procedures to surface disputes (on charges) to DSAA. (p. 15, GAO Draft Report).

Now on p. 11.

DoD Position: Partially concur. To the extent that the dispute applies to MDE items, DoD concurs. Disputes with regard to non-MDE items must be resolved within the applicable Military Department. (See, also, the DOD response to Finding F).

Advance Comments From the Department of State

United States Department of State

Comptroller

Washington, D.C. 20520

October 30, 1985

Dear Frank:

I am replying to your letter of September 27, 1985 to the Secretary which forwarded copies of the draft report: "Problems in Identifying, Monitoring, and Collecting Nonrecurring Charges Owed to the U.S. Government."

The enclosed comments on this report were prepared in the Bureau of Politico-Military Affairs.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,

Roger

Roger B. Feldman

Enclosure:
As stated.

Mr. Frank C. Conahan,
Director,
National Security and
International Affairs Division,
U.S. General Accounting Office,
Washington, D.C. 20548

GAO DRAFT REPORT: PROBLEMS IN IDENTIFYING, MONITORING, AND COLLECTING NONRECURRING CHARGES OWED TO THE U.S. GOVERNMENT

Now on p. 2, para. 4

In the interest of accuracy, it is recommended that the first paragraph on page 3 of the draft GAO report be amended as follows:

"The Department of State, as of September 30, 1985, approved 28,869 permanent export licenses and manufacturing license/technical assistance agreements received in fiscal year 1983 totaling about $10 billion in projected sales. Deliveries made against these approvals amounted to $3.9 billion as of September 30, 1985. With regard to permanent export licenses and manufacturing licensing/technical assistance agreements received during fiscal year 1984, a total of 33,344 has been approved totaling some $12 billion in projected sales. Deliveries against these approvals have amounted to some $2.8 billion as of September 30, 1985."

Now on p. 11.

With regard to the fourth recommendation contained on page 15 of the draft GAO report, the Office of Munitions Control, Department of State, will establish procedures ensuring that copies of all permanent export licenses and manufacturing licensing agreements involving more than $1 million will be forwarded to the Department of Defense for onward transmittal to the appropriate military service.

H. Allen Holmes
Director
Bureau of Politico-Military Affairs

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